

BEFORE THE
POSTAL REGULATORY COMMISSION
WASHINGTON, D.C. 20268-0001

ANNUAL COMPLIANCE REPORT, 2012

Docket No. ACR2012

REPLY COMMENTS OF THE ASSOCIATION FOR POSTAL COMMERCE

Pursuant to Commission Order No. 1609, the Association for Postal Commerce ("PostCom") hereby submits these reply comments in response to the comments filed by various parties on the Postal Service's Annual Compliance Report for Fiscal Year 2012 ("FY 2012 ACR"). PostCom submits these comments primarily to address the issue of Standard Mail Flats pricing and that product's failure to cover its costs during Fiscal Year 2012. For the practical and legal reasons discussed below, PostCom submits that prudence dictates that the Commission find Standard Mail Flats rates in compliance with the PAEA. To the extent any action should be taken regarding the Standard Mail Flats product, the Commission's order approving the amended rates for this product in Docket No. R2013-1 adequately addressed the issue.

Several parties addressed the Standard Mail Flats issue in their initial comments.¹ In particular, Valpak and the Public Representative urged the Commission to require the Postal Service to take more aggressive steps to achieve full cost coverage for the Standard Mail Flats product. *See* Valpak Comments at 122 (advocating price increases of 5% above CPI); Public

¹ *See, e.g.*, Comments of the Direct Marketing Association Responding to Commission Order No. 1609 at 1-2 ("DMA Comments"); Initial Comments of the American Catalog Mailers Association (ACMA); Public Representative Comments at 30-39; Valpak Direct Marketing Systems, Inc. and Valpak Dealers' Association, Inc. Initial Comments on the United States Postal Service FY 2012 Annual Compliance Report at 31-107 ("Valpak Comments").

Representative Comments at 39 (advocating price increases of 2-3% above CPI). PostCom submits that such action is unwarranted at this time.

The “underwater” status of the Standard Mail Flats product is not a new phenomenon, and there is nothing in the latest information submitted by the Postal Service that suggests there are new contours to this situation. Rather, the situation presented by the Postal Service in the FY 2012 ACR is a continuation of that presented in the ACR2010 docket, where the Commission found Standard Mail Flats to be out of compliance with the PAEA and ordered the Postal Service to take remedial action. Since that order, the Commission has had numerous opportunities to evaluate the steps the Postal Service is taking to bring Standard Mail Flats toward total cost coverage. When the Commission has found the Postal Service’s actions to be lacking, as it did in Order No. 1573 in R2013-1, it has ordered the Postal Service to take additional steps.

Notably, in Order No. 1573—issued just two months ago—the Commission determined that “the proposed Standard Mail price changes appear to comply with applicable Commission directives as required by Order No. 1541.” Order No. 1573 at 5. Importantly, the Commission clarified that “[a]lthough Valpak and the Public Representative take issue with the amount of the price increase, the Commission concludes that these rates comply with the FY 2010 ACD directives.” *Id.* The state of Standard Mail Flats has not changed since December. Further, there is no information in the FY 2012 ACR suggesting that the information the Commission relied on in reaching its conclusions in Order No. 1573 was outdated or inaccurately portrayed the Postal Service’s financial condition. Accordingly, a finding of noncompliance for the Standard Mail Flats product in this docket would be arbitrary and capricious.

Further, as PostCom explained in its initial comments in R2013-1, organic changes within the industry counsel for delaying any action to improve Flats coverage beyond that

achieved by the above-CPI price increases the Postal Service has indicated it will implement through Fiscal Year 2016. Ultimately, the low cost coverage of the Standard Mail Flats Automation product may be a problem that resolves itself. The entire discussion of whether the rate increases implemented by the Postal Service do enough to move Standard Flats closer to break even misses a fundamental change that is occurring in the mix of mail. Specifically, due to existing price incentives and improvements in co-mailing and co-palletization, a substantial portion of flats volume – including catalogs – has migrated from Standard Mail Flats to Carrier Route.

PostCom members have indicated that nearly 70% of catalog mail is now being sent as Enhanced Carrier Route. The billing determinants submitted by the Postal Service in this docket and data from RPW reports support this anecdotal evidence. Most noticeably, the RPW Report for Fiscal Year 2012 shows a 12.4% decrease in Standard Mail Flats volume over FY 2011 while Carrier Route volume decreased by only 2.3% over the same time period. This trend is apparent going back to 2010: even though there were declines in both categories of mail for much of this time period, Carrier Route volumes declined at a significantly lower rate. *See, e.g.*, RPW Report for Q2 FY 2012 (Year-to-date declines over the same period of FY2011 of 13.6% for Flats and only 8.4% for Carrier Route); Final RPW for 4Q 2010 (showing declines of 10.1% for Flats and only 5.3% for Carrier Route over FY 2009 volumes).

The price incentives contained in the R2013-1 rates are likely to continue this shift. The price gap between 5-digit Automation Flats and Carrier Route Flats widens from 8.2 to 8.3 cents under the new rates. *See* Notice 123, Price List, effective Jan. 27, 2013. Though the Postal Service maintains that it does not intend to allow this gap to increase in the future, the proposed differential will likely incent additional Flats pieces to move to Carrier Route.

In addition to the rate differential, these volume shifts are attributable to increased co-mailing and co-palletization by catalog mailers. As long as the incentives for these activities remain in place, the migration of Flats to Carrier Route should continue. Accordingly, rather than attempt to micromanage Flats and Carrier Route prices to achieve a predetermined result, the Commission should allow this migration to continue organically. Once it has run its course, the Commission can evaluate the effects of this migration and determine whether, and if so, what, further action is necessary to achieve the purposes of the PAEA.

The fact is that due to co-mailing, co-palletization, and price incentives, the migration to Carrier Route has been occurring and will continue to occur. As the Direct Marketing Association indicated in its initial comments, Standard Mail Flats are often residual pieces of a larger mailing. DMA Comments at 1. That is, when some of the pieces of a mailing cannot meet the eligibility requirements for Carrier Route Flats, the mailer will send these residual pieces as Standard Mail Flats. Since these pieces would not be sent on a stand-alone basis, the proper metric for evaluating cost coverage in this context is that of the overall mailing—the pieces that are mailed as Carrier Route as well as Standard Mail.

Finally, as detailed in the FY 2012 ACR, the cost coverage of Standard Mail Flats actually improved in Fiscal Year 2012 despite the continuing decline in Standard Mail Flats volume. FY 2012 ACR at 15. This is in direct contrast to past ACRs which showed a decline in volume and an increase in unit costs due to the fixed network of the Postal Service. This cost coverage improvement indicates that the cost reduction initiatives the Postal Service continues to pursue for both flats and its overall network reduction are beginning to show results. Accordingly, it is difficult to see why the Commission should take additional action *now*. PostCom submits that the more prudent course is to allow time for the cost reduction initiatives

to be fully implemented and for the pre-determined above-average price increases for Standard Mail Flats approved in R2013-1 to have an effect. The R2013-1 rates were just implemented on January 27 and have not yet had a chance to influence the cost coverage of Standard Mail Flats. At the end of this fiscal year, the Commission can evaluate, with better data, the effects of the Postal Service's initiatives on Standard Mail Flats volumes and cost coverage. To the extent the Commission does take action, it should direct the Postal Service to track the migration of Flats to Carrier Route, study the causes and effects of this migration, and only take such action as is warranted once a clearer picture of the future mailing patterns of catalogs and other Flats mailers emerges.

Respectfully submitted,

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